tried to find fault with the criteria it contained, in order to avoid making payment. The principle of sovereignty required the consortium to abide by the law of the land under which the letter of credit had been issued. It had in the end admitted its mistake and paid what it was required to pay. None the less, that example illustrated the problems of the beneficiary, which the Commission in its present discussion was neglecting in favour of those of the issuer. A satisfactory solution would be one which guaranteed the rights of both parties.

The meeting rose at 12.30 p.m.

Summary record of the 556th meeting

Monday, 8 May 1995, at 2 p.m.

[A/CN.9/SR.556]

Chairman: Mr. GOH (Singapore)

Chairman of the Committee of the Whole: Mr. GAUTHIER (Canada)

The meeting was called to order at 2.10 p.m.

DRAFT CONVENTION ON INDEPENDENT GUARANTEES AND STAND-BY LETTERS OF CREDIT *(continued)* (A/CN.9/405, A/CN.9/408 and A/CN.9/411)

Article 19 (continued) (A/CN.9/408, annex)

1. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that opinion in the Commission seemed to be divided almost equally and invited those delegations that had not spoken to take the floor. New ideas would also be welcome.

2. Mr. ILLESCAS (Spain) pointed out that there were two different sets of circumstances which should be more broadly recognized in the Convention. The cases covered by paragraphs (1)*(a)*(i) and (ii) involved facial conformity, where there was a clear duty not to pay on the basis of non-fulfilment of earlier articles of the Convention. In subparagraph (iii), on the other hand, facial conformity did not arise and a bank was given the possibility not to pay, with all the attendant consequences. In that context, the possibility of withholding payment, where the bank would have to take the decision following normal standards, could be recognized unreservedly.

3. Paragraphs (2)*(a)*, *(b)*, *(c)* and *(d)* listed circumstances where, despite facial conformity, the guarantor might entertain doubts regarding the basis of the demand, so that payment should be withheld.

4. He thought the term "discretion" was inappropriate because, in Roman law countries, it had the connotation of arbitrariness. In other respects, he supported the solution proposed by the delegation of the United States of America.

5. Mr. EDWARDS (Australia) said that he also had tried to establish a dichotomy between two sets of circumstances, the first in which payment should be withheld and the second in which there should be a right to withhold payment.

6. He proposed amendments to article 19:

Paragraph (1)*(a)* should be deleted and replaced by the following:

"(1) *(a)* If, at the time of presentation of the demand to the guarantor, there is information before the guarantor from which it is manifest and clear that:

(i) Any document is not genuine or has been falsified;

(ii) No payment is due on the basis asserted in the demand and the supporting documents; or

(iii) The demand has no conceivable basis,

the guarantor shall withhold payment to the beneficiary."

Paragraph (1)*(b)* should be deleted and replaced by the following:

"(1) *(b)* If, at the time of presentation of the demand to the guarantor, the guarantor is of the view that there is a high probability that:

(i) The document is not genuine or has been falsified;

(ii) No payment is due on the basis asserted in the demand and the supporting documents; or

(iii) The demand has no conceivable basis,

the guarantor shall have the right to withhold payment to the beneficiary."

The reference in paragraph (2) to paragraph (1)*(a)*(iii) should be deleted and replaced by "paragraph (1)*(a)*(iii) or (1)*(b)*(iii).".

A new paragraph (3) should be inserted to read:

"The action of the guarantor in withholding payment under paragraph (1)*(a)* or (1)*(b)* does not prejudice any rights of the principal or the beneficiary against the guarantor in respect of that action."

7. He explained that he had suggested deleting the words "judging by the type and purpose of the undertaking" from (iii) because they added little to the sense.

8. The purpose of the amendment to paragraph (1)*(a)* was to define what matters were left to the judgement of the guarantor and to specify that the guarantor was expected merely to make a decision on the basis of the documents before him and was not expected to make a search.

9. Mr. BONELL (Italy) commended the Australian proposal but asked for an explanation of the purpose of the new paragraph (3). That paragraph made sense in the type of situation in which payment might be refused if there were good reasons to do so; however, in a situation where there was a duty not to pay, he did not understand that such a duty could be subject to the condition that the case might later be reopened.

10. Mr. EDWARDS (Australia) said that while paragraph (1)*(a)* reduced the need for judgements on facts, such judgements nevertheless had to be made by the guarantor. The reason why paragraph (3) dealt with situations covered by paragraph (1)*(a)* and (1)*(b)* was that the guarantor might in the course of time be found to have been wrong. The provision was intended to ensure that the financial transaction could proceed with certainty in the commercial market-place. Withholding payment would permit subsequent correction in the case of such an error. However, the occurrence of an error and damage to the principal or guarantor should not prejudice recourse to law.

11. Ms. FENG Aimin (China) suggested that, if paragraph (1) of article 19 were incorporated in article 20, it might constitute a rule on the obligation to be undertaken by the bank. Article 19 merely stipulated that a bank did not pay or withheld payment in accordance with article 20. Her suggestion would mean that the stipulation would be aligned with UCP 500 rules, which did not give the bank the right not to pay.

12. Mr. FAYERS (United Kingdom) welcomed the Australian proposal, which, by its structure, well differentiated between a decision to be made at the time of presentation of a demand and the relevance of such a decision in subsequent later litigation.

13. The purpose of paragraph (3) was to protect the rights of the principal or beneficiary against the guarantor at such a later time, when payment had been withheld, in which case the beneficiary would presumably be the aggrieved party, so that it was difficult to see what rights of the principal needed to be protected in that context.

14. It might be desirable to cover the situation mentioned in paragraph (1)*(b)* in which the guarantor had the right to withhold payment but decided to pay. In that case the principal, who did not wish his account to be debited, had a right that should be protected.

15. The proposed paragraph (3) seemed to postulate withholding of payment, so that the rights of the beneficiary would not ultimately be prejudiced, and it was not clear what rights of the principal would be infringed.

16. Mr. STOUFFLET (France) commended the Australian proposal.

17. Paragraph (1)*(b)* would recognize the possibility, not the obligation, that the guarantor would refuse or defer payment when there seemed to him to be a high probability of irregularity. That would, however, derogate from the current practice of courts and the approach advocated in legal writing, which required certainty rather than high probability as the grounds for refusal of payment. The question of high probability also had some bearing on article 20.

18. The CHAIRMAN, speaking in his capacity as the representative of Singapore, supported the Australian proposal.

19. It should perhaps be made clear that, in order to prevent the perpetuation of fraud, the withholding of payment would not prejudice the right of a beneficiary to bring the matter to court.

20. Mr. GAUTHIER (Chairman of the Committee of the Whole) said that the Commission should now choose between three options.

21. The first was to adopt the Australian proposal, which provided that the bank either must or might withhold payment or had a right to do so. In that context, the United Kingdom had made a valid point, which would require drafting changes.

22. The second option, on the basis of the United States proposal, would be to provide that the guarantor/issuer, acting in good faith, had the right to withhold payment to the beneficiary if it were manifest and clear that either of the three circumstances described in subparagraphs (i), (ii) or (iii) of paragraph (1) were present.

23. The third option would be to retain the existing text of article 19, except that subparagraph (1)*(b)*(ii) would be deleted. That text would provide for an obligation not to make payment.

24. The passage "unless otherwise stipulated in the undertaking or agreed elsewhere by the guarantor/issuer and the beneficiary", which was in square brackets, might still have to be discussed.

25. Mr. SHISHIDO (Japan) said that the words "guarantor/issuer acting in good faith" should be added after the words "against the beneficiary" so as to make it clear to whom the guarantor/issuer was acting in good faith.

26. Mr. VASSEUR (Observer for Monaco) said that it was difficult to choose between the three options outlined by the Chairman without written texts. He thought that discussion of article 19, a key provision, should be suspended until those written texts were available for discussion.

27. Mr. GAUTHIER (Chairman of the Committee of the Whole) noted that there seemed to be a plurality in favour of the second option, which might therefore be considered as agreed. He suggested that the Commission move on to the consideration of article 20.

28. A brief procedural discussion followed, in which Mr. BONELL (Italy), Mr. LAMBERTZ (Observer for Sweden) and Mr. GAUTHIER (Chairman of the Committee of the Whole) participated.

Article 20 (A/CN.9/408, annex)

29. Mr. VASSEUR (Observer for Monaco) pointed out that, in the view of many member associations of the Banking Federation of the European Union, which he was also representing at the current session, article 20 was unnecessary, primarily because it was a procedural article and questions of procedure should be dealt with under national law and not in the Convention. When the Working Group had discussed rules on conflict of laws at its January 1995 session in New York, procedural questions had arisen and the relevant chapter had been eliminated.

30. Though article 20 on provisional court measures dealt with procedural questions, it had significant gaps; for instance, it did not state whether an appeal against such measures would be possible, whether rulings would be handed down at the mere request of the principal/applicant or after due hearing of the parties, and so on.

31. Secondly, very serious concern regarding article 20 had been expressed in a letter from the Banking Federation of the European Union to the Secretary. One of the most important banking associations in the Federation had stated that article 20 should be deleted because the criteria that it set forth were much less strict than the minimum rules in force permitting provisional court measures in most States of the European Union. Also, in all States of the European Union high probability was not a sufficient criterion.

32. Article 20, if retained, would encourage a principal/applicant to refer a matter to the judge in order to gain time, even if the action had little chance of success.

33. There was inconsistency between the provisions of articles 19 and 20, since article 19 used the phrase "manifest and clear",

whereas article 20 referred merely to "high probability". He therefore proposed, on the assumption that article 20 were retained, that a passage to the effect that a provisional court measure could be issued by the judge when it was manifest and clear, or indubitable or beyond doubt that one of the cases referred to in paragraph (1) of article 19 was present. If the reference to high probability were retained, there should be a new provision stipulating that, on rejection of a request for a provisional court measure by the principal/applicant, the latter be automatically ordered to pay damages; as a result, it would be aware that it should not use article 20 in order to gain time. The prohibition of preventive requests under article 20 was objectionable, because that was a matter for local law.

34. Provisional court measures should be taken only in exceptional circumstances, in which context the criterion that otherwise the principal/applicant would be likely to suffer serious harm was inadequate. The principal/applicant should be expected to know what it was doing. In the context of provisional court measures, it should be stated that the court not only could request the applicant to provide security but must do so.

35. He had for some years been drawing attention to the question of counter-guarantees and it was regrettable that article 20 ignored the situation of the bank as a counter-guarantor in the event of provisional court measures against the first bank, and also the situation of the first bank in the case of provisional court measures against the counter-guarantor bank. Article 20 should firmly state that provisional measures regarding the first guarantee should have no impact on the counter-guarantee, and conversely that such measures regarding the counter-guarantee should have no impact on the first guarantee.

The meeting was suspended at 3.35 p.m. and resumed at 4.05 p.m.

36. Mr. GAUTHIER (Chairman of the Committee of the Whole) invited the Commission to continue its consideration of article 20.

37. Mr. HARADA (Japan) said that, in his delegation's view, article 20 was unnecessary and should be deleted, for the following reasons. Firstly, there should be no interference with the court's discretion to decide whether or not to issue a provisional order and to decide what was the most appropriate type of order in the light of all the circumstances surrounding the case. Secondly, there should be no infringement of the court's freedom to evaluate the evidence. Thirdly, Japan had no restrictions on provisional measures such as were provided for in article 20, with respect to bills of exchange and promissory notes, even though the holder of such instruments might deserve greater protection than the beneficiary of the undertaking in the Convention.

38. If the proposal for outright deletion was not acceptable, his delegation would propose that the words "there is a high probability that" and "strong" in paragraph (1) and the whole of paragraph (3) should be deleted.

39. If that alternative proposal was not acceptable, either, his delegation would favour a reservation clause like article 22 of the Vienna Convention on the Sale of Goods.

40. Mr. CHOUKRI SBAI (Observer for Morocco) said that the provisional court measures provided for in article 20 were in conformity with his country's judicial system. If the procedure was abused, the party concerned would be liable for damages in respect of any delay in execution of the obligation. The provisions included in the article offered adequate safeguards: the need for "strong evidence", the consideration that the principal/applicant would be likely to suffer "serious harm" and the fact that the court could require the person applying to furnish security. The measures were intended to be available in relation to the cases dealt with in article 19(1)*(a),* where the beneficiary was at fault, but they could also protect the beneficiary against the consequences of any deal between the principal/applicant and the guarantor, particularly if the latter was a bank, since banks sometimes opted not to protect their clients from damage. The beneficiary would be able to plead before the court that the allegations by the principal/applicant were not well founded. The court would then have discretion as to what course to adopt.

41. Ms. CZERWENKA (Germany) said that article 20 left many issues to be decided by courts under their national laws. For instance, as it stood, the principal/applicant could apply for provisional court measures even if it had no claim against the guarantor/issuer. Under German law, that was not possible. However that might be, the basic rule was appropriate, namely, that the principal/applicant should have the possibility of applying for such measures. Nevertheless, she agreed with the Japanese representative that the references to "high probability" and "strong" evidence should be deleted. She also thought it unnecessary to provide for the possibility of blocking the proceeds of the undertaking already paid to the beneficiary, which lay outside the sphere that the Convention was intended to regulate.

42. Mr. STOUFFLET (France) said that the introduction of the "high probability" criterion looked like a withdrawal from the position that seemed to have been definitively established in a number of legal systems. Paradoxically, referring to evidence as "strong" might indicate some degree of laxity; it would be more forceful to refer to "immediately available" evidence.

43. He wondered whether the question of counter-guarantees affected only article 20, or whether it was not also relevant to article 19. If the latter, it might be desirable to have a separate article on the subject. The problem was a real one, and it would be unfortunate if it were ignored in the Convention.

44. Mr. LAMBERTZ (Observer for Sweden) said that it was difficult for him to take a position on article 20 without knowing what the final form of article 19 would be. The Working Group had provided for a lower level of proof in article 20, as reflected in the phrase "high probability", on the understanding that article 19 would be a "shall" rule. If, however, article 19 was to become a "may" rule, the link between the two articles would not be clear.

45. Mr. KOZOLCHYK (United States of America) said that the lower degree of proof implied by the phrase "high probability" was what was required when a petitioner was making an initial application for a temporary restraining order. The judge would require a higher level of proof when he came to decide whether to grant an injunction or not. It was proof of the latter sort that seemed to be at issue in article 20, so that the position taken by the representatives of France, Germany and Monaco seemed to be right. It was also in line with the way the Working Group had seen the matter.

46. Mr. BONELL (Italy) said that, notwithstanding that explanation, he agreed with the observer for Sweden that there was a logical link between article 19 and article 20. If the "shall" provision was retained in article 19, the formula in article 20 was correct. If, on the other hand, article 19 was a "may" rule, the scope of article 20 should be narrowed, deleting the references to "high probability" and "strong evidence", so that a reference to "immediately available evidence" should suffice.

47. Ms. FENG Aimin (China) said that the Commission should consider the suggestion made by the representative of Japan. The restrictions on the court under paragraph (3) of article 20 were too severe. The Commission should also consider the relationship between articles 19 and 20.

The meeting rose at 5 p.m.